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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

December 19, 1996

John Staurulakis, Inc.
6315 Seabrook Road
Seabrook, Maryland 20706

Secretary
Federal Communications Commission
1919 M Street, Room 222
Washington, D. C. 20554

In the Matter of	)	
	)	
Federal-State Joint Board on Universal Service	)	**CC Docket No. 96-45**
	)	
	)	

The accompanying comments, prepared by John Staurulakis, Inc. (JSI), are in response to the Public Notice, released November 18, 1996, in the above-referenced docket.

Any questions concerning this filing may be directed to JSI.

Sincerely,

Michael S. Fox
Director
Regulatory Affairs

Enclosures

cc: International Transcription Services, 2100 M Street, Room 140

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Before the
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Washington, D.C. 20554

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Comments of John Staurulakis, Inc.

Michael S. Fox
Director, Regulatory Affairs

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6315 Seabrook Road
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Date: December 19, 1996

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<u>Summary</u>

John Staurulakis, Inc. ("JSI") hereby files these comments in response to the November 18, 1996 Public Notice released by the Federal Communications Commission ("Commission") concerning the Federal-State Joint Board on Universal Service ("Joint Board").

The objective of universally available, affordable local exchanges service, in all areas of the Nation, is a cornerstone of the Telecommunications Act of 1996 (the "Act"). JSI believes that the Commission must adopt a universal service support mechanism for high-cost-to-serve areas which ensures that the universal service principles, as enumerated in the Act, are fulfilled.

JSI believes that the application of forward-looking economic costs is an inappropriate basis for determining the cost of providing universal service in the areas served by rural telephone companies, and that its adoption will, in fact, undermine universal service.

Rural telephone companies should be allowed to continue to receive universal service support based upon their realized, embedded costs until the *regulatory contract,* rate-base rate-of-return regulation, <u>and its attendant service obligations</u>, are removed.

Furthermore, JSI contends that using the frozen historical requirements per line of the existing universal service fund, dial equipment minute weighting, and long-term support, as recommended by the Joint Board, is inappropriate and will also undermine universal service.

JSI recommends that a rural carrier's current and ongoing embedded costs be used in establishing the true cost of maintaining universal service. JSI also recommends that

all rural telephone companies be treated in a similar manner and be allowed to continue to use embedded costs for universal service fund calculations during and beyond the initial three-year period.

Additionally, JSI is concerned by the prospect of designing a proxy model that will accurately establish the cost of providing universal service for a rural telephone company. In order for proxy models to be viable, they must be able to accurately depict actual costs, and not result in inappropriate swings or shifts over time. To date, no such model exists. Indeed, there is serious question as to whether one will ever exist for rural, high-cost areas. JSI recommends that rural telephone companies be permitted the option to establish universal support levels based on the company-specific cost of providing universal service.

JSI also believes that the Commission should adopt a *Maximum-Shift Cap* to further ensure the predictability of universal support, from year-to-year.

Further, JSI contends that limiting universal service funding eligibility to primary residence and single-line business lines is neither advisable nor practicable. JSI is concerned that the Joint Board's recommendations with respect to rural telephone companies will result in immediate and large changes in the support rural telephone companies receive. The use of primary residence and single-line businesses as the only lines eligible to receive support will undermine, rather than promote, universal service.

Applying universal service support only to primary residence and single-line businesses in rural areas would also introduce significant, ill-advised, and unjustified competitive disruptions into the marketplace. Such a rule will result in numerous practical, administrative, and privacy problems. It will also create unacceptable and unintended competitive arbitrage situations that would provide competitive local exchange carriers with a tremendous, and ill-advised, competitive advantage for second lines and lines to secondary residences.

Additionally, JSI is concerned that the level of customer "interrogation" that would be required to determine whether a line is for a primary residence or a second home may indeed border on an invasion of privacy. Even if telephone companies are empowered to ask these potentially intrusive questions, customers will have a huge incentive to always indicate that it is their "primary" residence. Enforcement will be difficult and potentially very costly.

Finally, there are a number of unresolved administrative issues that must be addressed before final rules can be adopted.

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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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	)	
Federal-State Joint Board on Universal Service	)	**CC Docket No. 96-45**
	)	
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Comments of John Staurulakis, Inc.

John Staurulakis, Inc. ("JSI") hereby files these comments in response to the Public Notice, released on November 18, 1996 by the Federal Communications Commission ("Commission") in the above captioned proceeding.[1] JSI is a consulting firm specializing in financial and regulatory services to more than one hundred and fifty Independent Telephone Companies throughout the United States. JSI assists these companies in the preparation and submission of jurisdictional cost studies and Universal Service Fund ("USF") data to the National Exchange Carrier Association ("NECA"), and routinely prepares and files tariffs with the Commission on behalf of a number of these client companies. In that the proposals and questions raised in the Federal-State Joint Board ("Joint Board") Recommended Decision, adopted on November 7, 1996[2] will affect the jurisdictional cost recovery of its client companies, JSI is an interested party in this proceeding.

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1 See In the Matter of Federal-State Joint Board on Universal Service, Public Notice, CC Docket No. 96-45, DA 96 1891, released November 18, 1996 ("Public Notice").

2 See In the Matter of Federal-State Joint Board on Universal Service, Recommended Decision, CC Docket No. 96-45, Commission 96J-3, released November 8, 1996 ("Recommended Decision").

Universal service is a long-standing national objective of the Commission and the telecommunications industry. It is also now a cornerstone of the Telecommunications Act of 1996 (the "1996 Act").[3] Therefore, JSI believes that the Commission should move cautiously as it fulfills the mandates of the 1996 Act.

It is clear that Universal service remains a very critical public policy element of telecommunications in the United States, particularly in rural communities throughout the nation. Rural telephone companies rely heavily upon high-cost assistance mechanisms, such as the interstate universal service fund, dial equipment minute ("DEM") weighting and long-term support ("LTS") payments, to ensure affordable local service rates and maintain high quality service in the rural areas they serve. Consistent with the provisions of the 1996 Act, it is important that the Commission ensure that the rules fashioned to promote universal service in the United States do in fact promote and not undermine universal service.

The establishment of the reconstituted universal service fund has become even more important because of the need to price local interconnection arrangements based on the incumbent local exchange carriers' "costs" and to remove implicit support from access arrangements. In its August 8, 1996 Local Interconnection Order, the Commission confirmed this and stated its intention to complete access charge reform "before or concurrently with a final order on universal service."[4] If universal service is to be

[3] See Telecommunications Act of 1996, Pub. L. No. 104-104, Stat. 56 (1996) (to be codified at 47 U.S.C. sections 151 et seq.).

[4] See In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, First Report and Order, CC Docket No. 96-98, Commission 96-325 ("Local Interconnection Order").

maintained, the universal service fund must be created to ensure that the actual costs, as opposed to hypothetical costs, of providing universal service are recoverable.

I. Goals and Principles of Universal Service Support Mechanisms

The principles upon which universal service is to be based were clearly established in the 1996 Act. These principles are as follows:

> (1) QUALITY AND RATES- Quality services should be available at just, reasonable, and affordable rates.
>
> (2) ACCESS TO ADVANCED SERVICES- Access to advanced telecommunications and information services should be provided in all regions of the Nation.
>
> (3) ACCESS IN RURAL AND HIGH COST AREAS- Consumers in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas, should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas.
>
> (4) EQUITABLE AND NONDISCRIMINATORY CONTRIBUTIONS- All providers of telecommunications services should make an equitable and nondiscriminatory contribution to the preservation and advancement of universal service.
>
> (5) SPECIFIC AND PREDICTABLE SUPPORT MECHANISMS- There should be specific, predictable and sufficient Federal and State mechanisms to preserve and advance universal service.
>
> (6) ACCESS TO ADVANCED TELE-COMMUNICATIONS SERVICES FOR SCHOOLS, HEALTH CARE, AND LIBRARIES- Elementary and secondary schools and classrooms, health care providers, and libraries should have access to advanced telecommunications services as described in subsection (h).
>
> (7) ADDITIONAL PRINCIPLES- Such other principles as the Joint Board and the Commission determine are necessary and appropriate for the protection

> of the public interest, convenience, and necessity and are consistent with this Act.[5]

Clearly, these principles are intended to ensure that both urban and rural consumers have access to similar quality telecommunications services at comparably priced rates in all areas of the United States. However, JSI believes that in refashioning the universal service fund mechanism, the Commission must bear in mind, in particular, the third universal service principle which requires that rural consumers should have access to telecommunications and information services that are reasonably comparable to those services provided in urban areas, at reasonably comparable rates.

Additionally, the fifth principle, requiring specific and predictable support mechanisms " . . .to preserve and advance universal service" is also crucial for rural consumers. JSI is concerned that certain recommendations made by the Joint Board will serve to undermine, rather than enhance, universal service. In particular, as will be explained later in these comments, the application of the *forward-looking economic costs,* as presently defined and proposed by the Joint Board, and the use of proxy models for rural telephone companies may not allow for a predictable nor sufficient Federal mechanisms to preserve and advance universal service.

II. Embedded Cost is the Appropriate Standard for Rural Carriers

The Joint Board concludes that forward-looking economic cost is the appropriate standard for determining Universal Service support. They recommend this cost standard because of the belief that forward-looking economic cost will provide the appropriate

[5] See The 1996 Act, section 254(b).

signals for competitive entry, efficient investment and innovation. JSI respectfully disagrees with this conclusion for areas served by rural carriers and will demonstrate that the use of a forward-looking economic cost is inappropriate and potentially damaging for rural universal service policy. Furthermore, this section will describe why the use of current embedded costs are more appropriate than the frozen embedded cost calculation proposed by the Joint Board Recommended Decision. The Joint Board rejects embedded cost because "no statutory or economic reason exists for calculating high cost support based on embedded costs." [Paragraph 284] State commissions and regulatory authorities have effectively used actual or embedded costs for determining the level of universal service support for areas served by rural carriers. This policy has sound regulatory reasoning and is fully justified by regulatory economic practice.

Forward-Looking Economic Cost

When the Joint Board recommended a particular version of forward-looking economic cost as a basis for determining universal service support, it *de facto* recommended a price for those services under the purview of universal service policy. This is because of the way the Joint Board determines the level of universal service support a carrier is eligible to receive. The Joint Board's recommendations for a high-cost recovery system for high cost areas is to determine a benchmark of revenues for the local exchange carriers and then determine the forward-looking economic cost for local exchange carriers. The difference between the forward-looking economic cost per line and the revenue benchmark per line represents the amount of universal service support per line a LEC is able to receive. The determination of a forward-looking economic cost and the revenue benchmark therefore constitutes a gross revenue contribution per line that the LEC can receive. This is a *de facto* price for services covered under universal service policy.

JSI contends that the use of a hypothetical, optimized, forward-looking economic cost for universal service is not appropriate because it will violate the plain language of the 1996 Act, which ensures that customers in rural areas have access to telecommunications and information services available at rates reasonably comparable to rates charged in urban areas. Without adequate protections, the placement of a forward-looking economic cost mechanism connected with a national revenue benchmark will place state commissions in the awkward and precarious position of setting rates in rural areas which may violate this established principle of universal service while attempting to provide adequate incentives for investment in plant and equipment in rural areas.

Furthermore, the Joint Board recommendation is contrary to the express intent of Congress to promote facilities-based competition in markets that will support competition. In the Joint Board Recommended Decision [Paragraph 275], forward-looking economic cost is promoted on the basis of providing appropriate signals for entry, investment and innovation. However, the United States Court of Appeals, Eighth Circuit is in receipt of comments presented by the Regional Bell Companies ("RBOCs") and GTE which clearly state that the intent of Congress in the 1996 Act was to promote facilities-based competition.[6] As mentioned, the Joint Board Recommended Decision promotes forward-looking economic cost that undermines this intent because the use of forward-looking economic cost provides no incentive for competitors to provide facilities when they can obtain all the functions of existing facilities based upon the most efficient technology currently available.

It is evident that the market characteristics which exist in rural areas are even less accommodating to facilities-based local competition than the urban areas served by the RBOCs and GTE. This was recognized by Congress when specific provisions for areas served by rural carriers were given separate treatment in the 1996 Act. Congress' intent to promote facilities-based competition would appear to be predicated upon the concept that multiple facilities-based providers is the most desirable form of local exchange competition. However, Congress realized that areas served by rural carriers may still be best served by a single provider under regulatory oversight. This realization is evident when, in the 1996 Act, Congress gives specific authority to state commissions to determine if it is the public interest, convenience and necessity to allow more than one essential telecommunications carrier into an area served by rural carriers. Prior to a specific finding by a state commission, the presumption granted by Congress is that rural carriers still operate in a market characterized as a natural monopoly for wireline service and that special provisions are required under such because facilities-based competition is inefficient in this type of market.

Because of the reasons specified above, JSI contends that forward-looking economic cost is an inappropriate standard for rural carriers and that the adoption of the Joint Board Recommended Decision violates the intent and specific language of the 1996

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[6] See Brief for Petitioners Regional Bell Companies and GTE, In the United States Court of Appeals for the Eighth Circuit, No. 96-3321 (and Consolidated Cases), Iowa Utilities Board, et al v. Federal

Act. More importantly, its adoption will cause irreparable harm to universal service in many rural segments of the nation.

Embedded Cost

JSI is particularly distressed by the apparent disregard for the long-standing regulatory economic practice which has provided measurable and predicable universal service support in the past decade for rural carriers. The Joint Board states that "no statutory or economic reason exists for calculating high cost support based on embedded costs," [Paragraph 284] and therefore rejects the use of embedded costs for the calculation of universal support for rural carriers. We emphatically disagree with the Joint Board conclusion and note the long legacy of regulatory involvement both with the Commission and state commissions and regulatory authorities that have successfully used actual or embedded costs for determining the level of universal service support for areas served by rural carriers. Unlike the RBOCs and GTE, rural carriers by-and-large still operate under rate-base rate-of-return regulation with oversight and regulatory controls. The statement that there is no statutory reason for using embedded cost is simply incorrect. Most, if not all, states have volumes of rules and regulations which constitute the law of the land for those rural local exchange carriers under their jurisdiction. This existing regulatory control over rural local exchange carriers is not likely to diminish given the unique market structure wherein these rural local exchange carriers operate. The existing regulatory relationship that rural local exchange carriers have, which is

Communications Commission and United States of America, page 48.

different from the experience of the RBOCs and GTE, is a necessary regulatory contract with the state authorities as well as the Commission.

Rural carriers largely operate on a rate-base rate-of-return regulatory foundation and, in exchange, have a multitude of service obligations imposed by state commissions in order to ensure universal service. Absent the regulatory contract, wireline universal service would cease to be a reality for many rural subscribers.

The use of realized, embedded costs in determining universal service support is based upon a long-standing regulatory contract between local exchange carriers and regulatory authorities because of these service obligations. The failure to recognize that rural local exchange carriers currently operate under radically different regulations than the RBOCs is particularly distressing when envisioning the application of the Joint Board recommendations. JSI submits that rural local exchange carriers should rely upon an embedded cost-based universal service support mechanism until rate-base rate-of-return regulation, <u>and its attendant service obligations</u>, are removed and replaced with regulation similar to that experienced by RBOCs. Only when the rate regulation and service obligations are removed from rural carriers, if state commissions determine that this removal is in the interest of the public, should rural carriers begin a transition to universal service support similar to that of the RBOCs.

III. Embedded Costs, Rather than Historical Costs per Line, are Appropriate for Universal Service Fund Calculations for <u>All</u> Rural Telephone Companies

JSI recommends the use of embedded costs as the basis for establishing universal service requirements. Furthermore, JSI contends that using the frozen historical requirements per line of the existing USF, DEM weighting and Long Term Support, as recommended by the Joint Board [Paragraph 283], is inappropriate and, in fact, violates the mandates of the 1996 Act. JSI's recommendation is that a rural carrier's current and ongoing embedded costs be used in establishing the true cost of maintaining universal service.

As explained in Section II, above, JSI emphatically recommends that rural carriers should receive universal service support based upon an embedded cost methodology. This will allow rural carriers to recover their true realized embedded costs and, therefore, fulfill their universal service obligations to their rural customers. JSI also recommends that all rural telephone companies be treated in a similar manner and be allowed to continue to use embedded costs for universal service fund calculations beyond the initial three-year period recommended by the Joint Board. [Paragraph 283]

At paragraph 285 of the Recommended Decision, the Joint Board concludes that "rural companies operating in Alaska and insular areas should not be required at this time to use a proxy model until further review." (emphasis added) This action will permit rural telephone companies operating in Alaska to depend upon a reliable and predictable universal service fund so that they can continue to provide comparable service to their customers, as required by the 1996 Act. JSI supports this recommendation, with the modification that the embedded formula to be used should be based on current embedded costs rather than the frozen calculation per loop recommended by the Joint Board.

JSI questions, however, why rural telephone companies operating in Alaska are inherently different from rural telephone companies throughout the United States that provide service in high-cost areas. For example, based upon 1995 data submissions made by the National Exchange Carrier Association ("NECA") to the Commission with respect to 1997 universal service fund payments, Wyoming reported 271,667 access lines while Alaska reported 360,287 (almost 90,000 fewer loops than Alaska).[7] Wyoming's 1995 reported unseparated cost per loop was $380.25. In comparison, Alaska's 1995 reported unseparated cost per loop was $382.65 (a mere $2.40 higher than Wyoming's). Furthermore, a review of NECA's 1996 submission of the 1995 Universal Service Fund study results to the Commission demonstrated that forty-three (43) states have at least one rural telephone company that reported higher unseparated costs per loop than at least one rural telephone company in Alaska. Therefore, why should rural telephone companies in Wyoming and other high-cost areas of the United States be treated differently than companies providing similar services in Alaska?

For the reasons previously noted, JSI recommends that all rural telephone companies be treated in a similar manner and be allowed to continue to use embedded costs for universal service fund calculations during and beyond the initial three-year period.

IV. Proxy Models will be Inherently Unpredictable for Rural Companies

At paragraph 277 of the Recommended Decision, the Joint Board proposes that the following criteria be used by the Commission to evaluate the reasonableness of any proxy model that would estimate the forward-looking economic costs of universal service:

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[7] See Universal Service Fund (USF) 1996 Submission of 1995 Study Results by the National Exchange Carrier Association, Inc., October 1, 1996.

(1) Technology assumed in the model should be the least-cost, most efficient and reasonable technology for providing the supported services that is currently available for purchase, with the understanding that the models will use the incumbent local exchange carriers' wire centers as the center of the loop network for the reasonably foreseeable future.

(2) Any network function or element, such as loop, switching, transport, or signaling, necessary to produce supported services must have an associated cost.

(3) Only forward-looking costs should be included. The costs should not be the embedded cost of the facilities, functions or elements.

(4) The model should measure the long-run costs of providing service by including a forward-looking cost of capital and the recovery of capital through economic depreciation expenses. The long run period used should be a period long enough that all costs are treated as variable and avoidable.

(5) The model should estimate the cost of providing service for all businesses and households within a geographic region. This includes the provision of multi-line business services. Such inclusion allows the models to reflect the economies of scale associated with the provision of these services.

(6) A reasonable allocation of joint and common costs should be assigned to the cost of supported services. This allocation will ensure that the forward-looking costs of providing the supported services do not include an unreasonable share of the joint and common costs incurred in the provision of both supported and non-supported services, e.g., multi-line business and toll services.

(7) The model and all underlying data, formulae, computations, and software associated with the model should be available to all interested parties for review and comment. All underlying data should be verifiable, engineering assumptions reasonable, and outputs plausible.

(8) The model should include the capability to examine and modify the critical assumptions and engineering principles. These assumptions and principles include, but are not limited to, the cost of capital, depreciation rates, fill factors, input costs, overhead adjustments, retail costs, structure sharing percentages, fiber-copper cross-over points, and terrain factors. The models should also allow for different costs of capital, depreciation, and expenses for different facilities, functions or elements.

As previously stated, JSI does not believe that it is possible to reconcile the use of forward-looking economic costs as the basis for establishing the universal service requirement with the mandate in the 1996 Act requiring a mechanism to provide the needed support to ensure that all consumers ". . . have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas." [Section 254(b)(3)] Likewise, JSI does not believe it is possible to reconcile the use of forward-looking costs with the mandate in the 1996 Act that requires that the mechanism should be specific, predictable and preserve and advance universal service.

Aside from JSI's significant concern about the use of forward-looking economic costs to define the true cost of providing universal service , as discussed in Section II, JSI is equally concerned about the prospect of successfully designing a proxy that captures the true cost of providing universal service in the areas served by rural telephone companies.

JSI believes that if proxies are approved for use as a surrogate for defining the cost of providing universal service, the Commission should also allow rural telephone companies to have the option of using actual company-specific "costs" for the calculation of universal service fund payments (however costs are ultimately defined).

While JSI is mindful of the potential complexity and expense of undertaking company-specific cost studies to establish universal service requirements, the specific mandates of the 1996 Act effectively require that such studies be conducted, regardless of cost, if they are necessary to allow rural telephone companies to continue to provide universal service. Moreover, such company-specific studies will be critical if universal support is to be "specific, predictable and sufficient," as required by the 1996 Act.

JSI believes that proxy models for rural carriers will prove to be unpredictable and will not capture the cost of providing universal service on a company-specific basis. The industry's efforts to date is clear proof of the complexity of the problem as it applies to the largest local exchange carriers. This is magnified for the small rural telephone companies.

For example, while the Joint Board did not advocate any specific proxy model, at this time, most proposed models utilize Census Block Group ("CBG") data in establishing the proxies. This is particularly problematic for rural telephone companies. JSI's experience is that CBGs are large geographic areas which inadequately identify the rural carriers' existing service territory. Literally, rural carriers may in some instances fall through the cracks with CBG data. This lack of reliability and consistency could prove disastrous for rural telephone companies. At best, relying upon any national proxy model could result in small, rural telephone companies experiencing periodic, and potentially significant, swings in universal service fund payments. This unpredictability is contrary to the 1996 Act, and would ultimately be detrimental to long-standing universal service principles.

If the Commission proceeds with the development of a proxy model for rural telephone companies, then it is imperative that rural telephone companies have the option of using actual company-specific "costs" for calculation of universal service fund payments. The concept of providing rural telephone companies with alternatives is well-established with the Commission.

For years, rural telephone companies have had the option of electing to develop their own costs for jurisdictional cost separation purposes, rather than rely upon the average schedules. Also, at paragraph 283 in the Recommended Decision, the Joint Board proposed that during the six-year transition, rural telephone companies be allowed to elect to use a proxy model to determine universal service fund support, rather than continue to receive support based upon historical, embedded costs. Allowing rural telephone companies to choose between different alternatives will better enable the Commission to meet the mandates of the 1996 Act, specifically the requirement that the universal service fund be specific, predictable and sufficient to advance universal service.

V. To Further Ensure Predictability, a Maximum-Shift Cap should be Established by the Commission

To ensure that the Joint Board's recommendation of short-term stability for rural telephone companies is achieved [paragraph 283], JSI also believes that if a proxy model is adopted, a "maximum shift or change" feature should be included to further ensure the predictability of the reconstituted universal service fund.

The concept of a maximum shift is not a novel idea, it has been used in this industry to mitigate separations and universal service fund changes. For example, Section §36.154(f)(1), of the Commission's rules, indicates that the study area interstate allocation of net Exchange Line Cable and Wire Facility investment, net Exchange Line Circuit Equipment Excluding Wideband investment and the associated maintenance and depreciation expenses shall not decrease by more than five percentage points from one calendar year to the next as a result of the Subscriber Plant Factor phasedown described in sections §36.154(d) and §36.641 (a) and (b) of the rules. This concept is similar to the way many adjustable rate mortgages ("ARMs") work. For example, many ARMs include a provision that the interest rate will not shift more than two percent (2%) at any time.

A similar maximum shift could be incorporated into a proxy model for rural telephone companies; *e.g.*, rural telephone companies electing to use a proxy model would not see their universal service payments increase or decrease by more than five percent (5%) per year. This would protect rural telephone companies and their customers from major shifts due to census changes, errors in census data or other factors. It would also provide rural telephone companies with the predictability and stability necessary to ensure that they are able to continue to invest in plant and equipment needed to provide universal service in rural America.

Such stability is not only important from a public policy perspective, but it is also mandated by the 1996 Act which requires "access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas." [Section 254(b)(3)].

VI. The Use of Primary Residence and Single-Line Business Loops to Establish Universal Service Support for Rural Telephone Companies Will Result in Immediate and Unpredictable Large Shifts

Aside from the problems caused by using an historical cost-per-line formula, as explained in Section III, JSI contends that the use of primary residence and single-line businesses as the only lines eligible to receive support will, in fact, undermine universal service.

At paragraph 283 of the Recommended Decision, the Joint Board indicates its concern with respect to large changes in rural telephone company universal service support. Specifically, the Joint Board is "concerned that moving small, rural carriers to a proxy model too quickly may result in large changes in the support that they receive." The Joint Board went on to point out that because "rural carriers generally serve fewer subscribers relative to the large incumbent local exchange carriers, serve more sparsely populated areas, and do not generally benefit from economies of scale and scope as much as non-rural carriers, they often cannot respond to changing operating circumstances as quickly as large carriers." JSI agrees with the Joint Board's concern in this regard. However, JSI is also concerned that the Joint Board's recommendations with respect to rural telephone companies will indeed result in immediate and large changes in the support rural telephone companies receive.

Paragraph 283, as well as 285, of the Joint Board's Recommended Decision indicates that the Joint Board clearly intended that the impact on rural telephone companies should be managed carefully in order to prevent unintended negative consequences for universal service in rural areas. Therefore, the application of the universal service rules must be consistent with this intent. For example, it would be completely contrary to this intent for the Commission to craft rules that determine a rural telephone company's 1997 universal service fund payments per loop based upon <u>all</u> 1995 loops but apply this per-loop figure only to future primary residence and single-line business loops. Paragraphs 290 through 295 of the Joint Board's Recommended Decision address the specific proposal for the calculation of the per-loop amounts of high-cost assistance, DEM weighting, and LTS payments. For example, the Recommended Decision is vague on whether the loop counts used in 1995 high-cost calculations are to be consistent with the application of these per-loop figures to future year high-cost fund payments.

If, contrary to JSI's recommendations in Section III, the Commission insists on using a frozen, historical per loop calculation, then at least it should allow all loops to be eligible for support in order to reduce the potential for under-recovery of rural carriers' actual costs.

To prevent immediate and unacceptable large shifts in universal service fund support to small, rural telephone companies, the denominator in the 1995 high-cost assistance calculations, as well as the 1996 DEM weighting and LTS payment calculations, must be consistent with the future application of these per-loop figures. To do otherwise would be contrary to the intent of the 1996 Act, as well as the intent of the Joint Board's Recommended Decision. The high-cost support per loop must be divided by 1995 "qualifying access lines."[8] DEM weighting support and LTS payments must

[8] Note: The correct formula for calculating the 1998 high cost assistance is as follows:

$$\frac{\$USF\ Funding_{1997}}{qualifying\ access\ lines_{1995}} = Funding\ Ratio\ for\ qualifying\ access\ lines_{1997}.$$

By extension, the funding ratio is to be used for future years in the following manner: (using 1998 as an example) similarly be divided by 1996 qualifying access lines. Paragraphs 88 through 92 of the Recommended Decision effectively define qualifying access lines as the initial primary residence and single-line business customers. JSI has serious practical and operational concerns with limiting universal service fund payments to these qualified access lines. The cost to provide service to all lines does not vary significantly from the cost of providing service to primary residential line and single-line businesses, particularly for rural telephone companies operating with carrier-of-last-resort obligations. However, if the Commission proscribes that these are the only access lines to receive universal service fund support, they must be the basis for the respective denominators in the frozen per-loop calculations of high-cost, DEM weighting and LTS support.

To do otherwise would subject many rural carriers to immediate and unacceptable consequences. For example, a JSI client, that we believe is fully representative of similar small, rural telephone companies serving high-cost areas of the country, serves approximately 5,500 access lines in a rural, high-cost area of the country. Using assumptions based upon the Joint Board's Recommended Decision for prospective 1998 universal service fund, DEM weighting and LTS support, this company would experience an immediate drop of almost $1 million its total high-cost assistance in 1998; an impact of more than $15.00 per month per loop. The 1997 frozen universal service assistance per-loop figure was derived by dividing anticipated 1997 universal service payments by <u>total</u> 1995 loops and applying this figure only to <u>qualified</u> 1996 loops. The anticipated assistance for DEM weighting and LTS were similarly calculated using <u>total</u> 1996 loops

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$$\textit{Funding Ratio for qualifying access lines}_{1997} * \textit{qualifying access lines}_{1996} = \$\textit{USF Funding}_{1998}$$